

STATE OF MINNESOTA
OFFICE OF ADMINISTRATIVE HEARINGS
FOR THE DEPARTMENT OF EDUCATION

In the Matter of the Termination of the
Existing Contract Between BlueSky
Online Charter School and Novation
Education Opportunities

**FINDINGS OF FACT, CONCLUSIONS,
AND ORDER ON APPLICATION FOR
ATTORNEYS' FEES AND COSTS
UNDER THE MINNESOTA EQUAL
ACCESS TO JUSTICE ACT**

The above-entitled matter is now pending before Chief Administrative Law Judge Raymond R. Krause on the application of BlueSky Online Charter School (BlueSky or School) for attorneys' fees and costs under the Minnesota Equal Access to Justice Act (MEAJA¹). BlueSky filed its application on March 19, 2012. The Department of Education (Department) filed its objection to the application on April 2, 2012. BlueSky filed a reply on April 24, 2012, and the Department filed a response to BlueSky's reply on April 25, 2012. The OAH record on the request for attorneys' fees closed on April 25, 2012.

Martha J. Casserly, Assistant Attorney General, represented the Department. Cindy Lavorato, Attorney at Law, Booth & Lavorato, LLC, represented BlueSky.

Based upon the submissions of the parties and for the reasons set forth in the attached memorandum, the Administrative Law Judge makes the following:

STATEMENT OF ISSUES

1. Is BlueSky a "party" within the meaning of the MEAJA?
2. Was BlueSky the "prevailing party" under Minn. Stat. § 15.472(a)?
3. Was the Department's enforcement action against BlueSky "substantially justified" within the meaning of Minn. Stat. § 15.472?
4. If not, is an award of attorneys' fees and costs of approximately \$282,000 warranted as provided by Minn. Stat. § 15.472?

Based on the evidence in the hearing record, the Administrative Law Judge makes the following:

¹ Minn. Stat. §§ 15.471—15.474. Minnesota Statutes are cited to the 2011 Edition.

FINDINGS OF FACT²

Background

1. BlueSky is a Minnesota public charter school organized as a nonprofit corporation pursuant to the Minnesota Charter School Law.³ BlueSky is also an approved online school provider.⁴

2. BlueSky has a Charter School Authorizer contract with Novation Education Opportunities (Novation), a nonprofit educational organization.

3. At all material times, BlueSky has had less than 500 employees and annual revenues that did not exceed \$7,000,000.⁵

4. Shortly after the Department certified BlueSky as an online learning provider in December 2008, it received complaints that alleged BlueSky's classes were not aligned with state standards and that students transferring from BlueSky were not prepared for their next course sequence. Based on these complaints, the Department began an investigation of BlueSky's curriculum to determine if BlueSky was in compliance with state academic standards and graduation requirements.⁶

5. The Department had never conducted a curriculum review of any school prior to BlueSky and there were no written procedures or policies in place to guide the curriculum review process.⁷

6. After more than two years of reviewing BlueSky's curriculum and graduation data, the Department concluded that BlueSky engaged in major and repeated violations of state law governing academic and graduation standards.

7. On April 21, 2011, the Department decided to terminate BlueSky's charter school contract. At the request of BlueSky, the Department set the matter on for hearing at the Office of Administrative Hearings.

8. A hearing in this matter was held before Chief Administrative Law Judge Raymond Krause on September 26-28, 2011. After the evidentiary hearing, Judge Krause issued a report and recommendation on November 21, 2011. Judge Krause concluded that, while BlueSky did violate certain academic standards and graduation requirements, the Department failed to establish by a preponderance of the evidence that BlueSky's non-compliance constituted a history of major or repeated violations of

² See, Minnesota Rule 1400.8401, subp.7 (2010). The Administrative Law Judge takes judicial notice of the entire record in this matter, including exhibits and testimony offered in the September 2011 contested case hearing. Accordingly, some of the Findings contained in this decision are derived from the record of the contested case hearing.

³ Minn. Stat. § 124D.10.

⁴ Minn. Stat. § 124D.095.

⁵ Substituted Affidavit of Donald Hainlen at ¶12 (filed April 9, 2012).

⁶ Commissioner of Education's Decision and Order, Finding No. 20 (February 16, 2012).

⁷ *Id.* at Finding No. 21.

law under Minn. Stat. § 124D.10, subd. 23(d). Judge Krause recommended that the Commissioner of Education dismiss the matter and rescind the Department's termination of the contract between BlueSky and its Authorizer Novation.

9. By Order dated February 16, 2012, the Commissioner accepted the ALJ's recommendation and rescinded the Department's action to terminate the charter school contract between BlueSky and Novation, and dismissed the matter on the grounds that the Department failed to demonstrate a history of major or repeated violations of law.

10. On March 19, 2012, BlueSky filed an application for attorneys' fees and costs under the MEAJA. The Department filed its objection to the application on April 2, 2012, and the record on the application closed with the filing of the parties' responses and replies on April 25, 2012.

CONCLUSIONS

1. BlueSky's motion for attorneys' fees and expenses is governed by the MEAJA and the rules of the Office of Administrative Hearings.⁸

2. BlueSky is a "party" as that term is defined by the MEAJA. BlueSky is a non-profit corporation with less than 500 employees and annual revenues of not more than \$7,000,000.⁹

3. BlueSky is the "prevailing party" in this matter.¹⁰

4. Under the MEAJA, if a prevailing party other than the state in a contested case proceeding shows that the position of the state was not substantially justified, the Administrative Law Judge "shall award fees and other expenses to the party unless special circumstances make an award unjust."¹¹

5. The term "state" is defined under the Act to mean the "state of Minnesota or an agency or official of the state acting in an official capacity."¹²

6. As a public charter school, BlueSky is part of the state's system of public education but it does not meet the definition of the term "state" for purposes of the MEAJA.

7. BlueSky has the burden of proving by a preponderance of the evidence that the Department's enforcement action in this matter was not substantially justified.¹³

⁸ Minn. Stat. § 15.471, *et seq.*; Minn. R. 1400.8401.

⁹ Minn. Stat. § 15.471, subd. 6.

¹⁰ Minn. Stat. § 15.472(a).

¹¹ Minn. Stat. § 15.472.

¹² Minn. Stat. § 15.471, subd. 7, and Minn. Stat. § 15.472(a).

¹³ Minn. Stat. § 15.472; Minn. R. 1400.7300, subp. 5. *See also, Donovan Contracting of St. Cloud v. Minnesota Department of Transportation*, 469 N.W.2d 718, 720 (Minn. App. 1991), *reviewed denied* (Minn. August 2, 1991).

8. BlueSky has failed to establish by a preponderance of the evidence that the Department's enforcement action was not substantially justified.

9. The Department is authorized to review a charter school's curriculum and to terminate a charter school's contract in the event of repeated or major violations of law.¹⁴

10. The Department's decision to terminate BlueSky's charter school contract and its conclusion that BlueSky engaged in major and repeated violations of state law governing academic and graduation standards had a reasonable basis in law and fact, based on the totality of the circumstances before and during the contested case proceeding, and was therefore substantially justified.¹⁵

11. These Conclusions are reached for the reasons discussed in the attached Memorandum, which is incorporated by reference.

Based on the Conclusions, the Administrative Law Judge makes the following:

ORDER

IT IS HEREBY ORDERED that:

BlueSky's Application for Attorneys' Fees and Costs is **DENIED**.

Dated: May 8, 2012

s/Raymond R. Krause

RAYMOND R. KRAUSE
Chief Administrative Law Judge

¹⁴ Minn. Stat. §§ 124D.095, subd. 7(b) and 124D.10, subds. 8(j) and 23(d).

¹⁵ See, Minn. Stat. § 15.471, subd. 8.

MEMORANDUM

Applicable Law

Under the MEAJA, if a prevailing party in a contested case proceeding shows that the position of the state was not substantially justified, the Administrative Law Judge “shall award fees and other expenses to the party unless special circumstances make an award unjust.”¹⁶

Because the Act is a limited waiver of sovereign immunity, its language must be strictly construed.¹⁷ “Party” is defined in a restrictive fashion in the Act to include only small businesses (those with not more than 500 employees and annual revenues not over seven million dollars) and partners, officers, shareholders, members, or owners of such entities.¹⁸ Recovery is available only in cases where the state’s position is represented by counsel and is not substantially justified.¹⁹ The word “state” is defined to mean “the state of Minnesota or an agency or official of the state acting in an official capacity.”²⁰ The phrase “substantially justified” is defined to mean that: “the state’s position had a reasonable basis in law and fact, based on the totality of the circumstances before and during the litigation or contested case proceeding.”²¹

Positions of the Parties

BlueSky has filed an application under the MEAJA seeking an award of attorneys’ fees and costs in the amount of \$283,200.70.²² In support of its application, BlueSky maintains that it is a “party” within the meaning of Minn. Stat. § 15.471, subd. 6, because it is organized as a nonprofit corporation, has less than 500 employees and annual revenues of less than seven million dollars. BlueSky also contends that it may proceed under the MEAJA because it does not meet the definition of the term “state” and that, as a public charter school, it is not one of the agencies specifically identified as a department of state government under Minn. Stat. § 15.01. BlueSky asserts further that it was the prevailing party in the matter since it prevailed on virtually every significant issue in the case.

BlueSky also argues that the Department did not have substantial justification for pursuing this action because the enforcement action lacked a reasonable basis in law and fact. BlueSky asserts that the Department pursued termination of BlueSky’s charter school contract without first establishing a clear process for such action through rulemaking. According to BlueSky, such conduct amounted to an invalid application of

¹⁶ Minn. Stat. § 15.472(a) (emphasis added).

¹⁷ *Donovan Contracting, supra*.

¹⁸ Minn. Stat. § 15.471, subd. 6.

¹⁹ Minn. Stat. § 15.472: *see also Donovan Contracting, supra*.

²⁰ Minn. Stat. § 15.471, subd. 7.

²¹ Minn. Stat. § 15.471, subd. 8.

²² In its Reply Brief, BlueSky stated that it is willing to reduce the total amount of fees requested by \$1,782 to account for some errors it discovered when reviewing its 30 pages of billings. With this reduction, BlueSky now seeks \$281,418 in attorneys’ fees and costs.

unpromulgated rules, which is not substantially justified in law.²³ In addition, BlueSky maintains that the Department lacked a reasonable basis in law for several of the “corrective action” items for which it cited BlueSky as violating. The Department later conceded that these were not required by law. BlueSky also asserts that the Department lacked a reasonable basis in fact because it did not conduct an adequate independent review of BlueSky’s curriculum to determine if violations occurred.

The Department argues that BlueSky is excluded from recovery of fees and costs under the MEAJA on several grounds. First, the Department argues that, as a public charter school, BlueSky is “part of the state’s system of public education”²⁴ and is a state actor making it ineligible to recover fees under the Act.²⁵ The Department maintains that in determining whether a charter school is a public entity, weight should be given to the fact that this proceeding arose out of BlueSky’s activities and responsibilities as a public charter school, not as a private vendor providing education services under contract as BlueSky claims. In addition, the Department asserts that the Commissioner of Education is immune from civil liability for all charter school activities under Minn. Stat. § 124D.10, subd. 25(c), including liability for any potential fees or costs of a charter school.

The Department also contends that the MEAJA only applies to contested case hearings required by law or constitutional right. The Act defines a “contested case” as “a proceeding defined in section 14.02, subdivision 3.”²⁶ Section 14.02, subdivision 3, in turn, defines a contested case hearing as “a proceeding before an agency in which the legal rights, duties, or privileges of specific parties are *required* by law or constitutional right to be determined after an agency hearing.”²⁷ The Department asserts that a contested case hearing was not required by law in this case. The Department points out that this matter arose under section 124D.10, subd. 23(d), which requires only a “public hearing.” According to the Department, the Commissioner granted the School’s request for a contested case hearing even though a formal hearing was not required. Because a contested case hearing under Chapter 14 was not required, the Department contends this matter is excluded from coverage under the MEAJA.

The Department also argues that BlueSky does not qualify as a “party” under the MEAJA because it is not one of the five entities listed as qualifying as a “party” under the Act. Specifically, the Department asserts that BlueSky is not “an unincorporated business, partnership, corporation, association, or organization.”²⁸ Although the Department concedes that, like all charter schools, BlueSky is statutorily required to be set up as a nonprofit corporation, the Department contends that it remains a public school and part of the State’s educational system.²⁹ The Department maintains that, as

²³ *Citing Donovan Contracting, supra.*

²⁴ Minn. Stat. § 124D.10, subd. 7.

²⁵ *See, Am. Civil Liberties Union of Minn. v. Tarek ibn Ziyad Acad. (TiZA)*, 2009 WL2215072 at *9 (D. Minn. July 21, 2009) (charter school is a “state actor” for civil rights violations).

²⁶ Minn. Stat. § 15.471, subd. 3.

²⁷ Minn. Stat. § 14.02, subd. 3 (emphasis added).

²⁸ Minn. Stat. § 15.471, subd. 6.

²⁹ *See, Minn. Stat. § 124D.10, subd. 4(a).*

a public school, BlueSky cannot claim recovery under MEAJA. According to the Department, the Act's legislative history makes clear that the intent of the statute was to protect small businesses from excessive regulators. The Department argues that the Act defines "party" in a restrictive fashion for that reason and it should not be expanded to include public schools, charter schools, or the state's system of public education.

The Department maintains that since BlueSky was not successful on every legal issue in the proceeding, it does not qualify as a "prevailing party." The Department notes that the Administrative Law Judge and Commissioner both concluded that BlueSky violated state academic standards and graduation requirements, but both concluded that a history of major violations of law was not shown. The Department also points out that BlueSky did not prevail on any of its key legal challenges regarding the Department's authority or the process and procedures it employed. The Department argues that in the end, BlueSky received only mixed results and should not be considered the prevailing party.

Finally, the Department argues that its position in this matter was substantially justified and had a reasonable basis in both law and fact. The Department points out that its attempt to terminate BlueSky's charter school contract was a case of first impression and, as such, there was no precedent to dictate the process or result. In addition, the Department notes that, while it did not achieve the relief it sought, both the Administrative Law Judge and the Commissioner concluded that the Department's actions were not arbitrary and capricious.

Analysis

The MEAJA was enacted as an exception to the general rule that parties bear their own costs of litigation. An Administrative Law Judge may award fees in a contested case proceeding to an eligible party if "the position of the state was not substantially justified . . . unless special circumstances make an award unjust."

BlueSky meets the threshold requirement for "party" status under the MEAJA. It is a nonprofit corporation with less than 500 employees and annual revenues that do not exceed seven million dollars. The statute does not distinguish between a non-profit corporation and a for-profit corporation. As a public charter school, BlueSky is part of the state's system of public education, however, it is not a state department or agency and under the plain language of the statute it does not meet the definition of the term "state." BlueSky is also the prevailing party in this matter because it succeeded on most of the significant issues in the case and the Department ultimately rescinded its termination of BlueSky's contract and dismissed the action.

The Administrative Law Judge is not persuaded by the Department's argument that the MEAJA only applies to contested case hearings that are *required* by statute or constitutional right. Whether or not a contested case was statutorily required in this matter, the Department subjected itself to the standards set forth in MEAJA by granting BlueSky's request for a contested case hearing.

BlueSky, however, has failed to show that the Department's enforcement action was not substantially justified. Instead, the Administrative Law Judge concludes that the Department's attempt to terminate BlueSky's charter school contract had a reasonable basis in law and fact based on the totality of the circumstances before and during the contested case. In *Donovan Contracting of St. Cloud, Inc. v. Minnesota Dept. of Transportation*,³⁰ the Minnesota Court of Appeals construed "substantially justified" to mean "justified to a degree that could satisfy a reasonable person" rather than "justified to a high degree." The Department's failure to prevail on the merits in the contested case proceeding does not, by itself, mean that its position was not substantially justified.³¹

BlueSky argues that *Donovan Contracting* definitively stands for the proposition that engaging in unpromulgated rulemaking which results in costs for a party is not "substantially justified in law" and that fees and costs for such action should be awarded under MEAJA. In *Donovan Contracting*, contractors successfully challenged the Minnesota Department of Transportation's (MnDOT) unilateral promulgation of an "Addendum A" interpreting the term "substantially in place" in the portion of the Minnesota Prevailing Wage statute applicable to highway construction contracts. The Court found MnDOT's attempt to enforce its Addendum A without first engaging in rulemaking did not have a reasonable basis in fact or law where MnDOT knew that the term was susceptible to more than one meaning and that interpretive rules must be adopted pursuant to rulemaking procedures.³²

This case is distinguishable from *Donovan Contracting*. In this case, the Department received complaints about BlueSky and began an investigation to determine if BlueSky was in compliance with state academic standards and graduation requirements. The Department is specifically authorized by statute to review a charter school's curriculum and to terminate a charter school's contract in the event of repeated or major violations of law.³³ The Department's efforts in reviewing BlueSky's curriculum were intended to implement and enforce existing law. The fact that the Department did not have written procedures in place to guide the curriculum review process, while troublesome, did not render the process invalid where the review was authorized by the statute itself.³⁴ In *Donovan Contracting*, on the other hand, MnDOT went beyond enforcing the mere terms of the statute. It published an addendum that purported to interpret statutory language and which had the general effect of extending the coverage of the Prevailing Wage Act to truck drivers on highway construction projects.³⁵ MnDOT's "Addendum A" was an interpretive rule that had the force and effect of law.³⁶

³⁰ *Donovan Contracting*, 469 N.W.2d at 720.

³¹ *Id.*

³² *Id.* at 721-723.

³³ Minn. Stat. § 124D.095, subd. 7(b) and 124D.10, subds. 8(j) and 23(d).

³⁴ See *Cable Communications Board v. Nor-west Cable Communications Partnership*, 356 N.W.2d 658, 667 (Minn. 1984); *Sellner Manufacturing Co. v. Commissioner of Taxation*, 202 N.W.2d 886, 888-89 (Minn. 1972) (If the agency action is authorized by the statute itself, the fact that no rule was adopted does not render the interpretation invalid.)

³⁵ *Donovan Contracting*, 469 N.W.2d at 722.

³⁶ *Id.*

The Court correctly held that the addendum was subject to rulemaking and that publishing it without first engaging in rulemaking was not a justified action for the state to take.³⁷

In this case, while the Administrative Law Judge stated in his recommended order that the review process “should be clarified through rulemaking,” he did not find that the Department engaged in invalid unpromulgated rulemaking. Moreover, an agency is permitted to formulate policy on a case-by-case basis following APA adjudication procedures, so long as the agency applies specific facts to specific parties.³⁸ Finally, both the Administrative Law Judge and the Commissioner concluded that the Department did not act arbitrarily in deciding to terminate BlueSky’s charter school contract. Therefore, contrary to BlueSky’s claim, the lack of a written curriculum review process did not render the Department’s action in this matter as lacking a reasonable basis in law or fact.

In the end, BlueSky was found to have violated some academic standards and graduation requirements. Although the Department failed to establish that BlueSky’s non-compliance amounted to repeated or major violations of law, the violations that were proven support a finding that the Department had a basis in law and fact for its actions. Considering the Department’s position in light of all the circumstances, the Administrative Law Judge concludes that the Department’s actions were substantially justified. BlueSky is not entitled to recover fees and costs under the MEAJA.

Because the Administrative Law Judge concludes that the position of the Department in this matter was substantially justified, it is not necessary to address the remaining arguments of the parties including the Department’s claim that the Commissioner’s immunity from civil liability for all charter school activities under Minn. Stat. § 124.10, subd. 25(c) encompasses claims brought under the MEAJA.

For the reasons set forth above, BlueSky’s request for attorneys’ fees and expenses is denied.

R. R. K.

³⁷ *Id.*

³⁸ *Bunge Corp. v. Commissioner of Revenue*, 305 N.W.2d 779 (Minn. 1981) (stating that agency may promulgate rules or make case-by-case determinations and that agency has discretion to decide which is appropriate under circumstances.); *L&D Trucking v. Minnesota Depart. of Transportation.*, 600 N.W.2d 734, 736 (Minn. App. 1999) (in case by case determinations, specific facts must be applied to specific parties); *Reserve Life Ins. Co. v. Commissioner of Commerce*, 402 N.W.2d 631, 634 (Minn. App. 1987) (finding it reasonable for commissioner to make statutory interpretations and decisions on case-by-case basis), *rev denied* (Minn. May 20, 1987).